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SIPDIS

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SUBJECT: Privatization Update: GOI Sells Israel Discount Bank

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Summary

1. (U) The Israeli government's privatization program is moving forward. On January 22, GOI Accountant General Yaron Zelka concluded an agreement with prominent businessman and Seagram heir Matthew Bronfman for the transfer of 26% of Discount Bank to the Matthew Bronfman group for a price of NIS 1.3 billion. Next step: Sale of Bank Leumi. End Summary.

IDB: Israel's Third Largest Bank

2. (U) A Brief History: IDB was established by Leon Recanati in 1935 and run by various members of the Recanati family until the mid-1980s. Following a general crash in bank share prices in 1983-1984, the GOI assumed control of the bank. As of the sale to Bronfman, the State owns 57.09% of the Bank's shares; the public 31.95%; while the remainder is in the hands of various Israeli mutual funds.

3. (U) Discount Bank's Place in the Market: Israel Discount Bank is the third largest Israeli bank, with assets of USD 32 billion at the end of 2003. In spite of its ranking, IDB lags far behind its main competitors, Banks Hapoalim and Leumi, in terms of market share.

4. (U) New York Branch the Key Asset: Although IDB has 120 branches in Israel, IDB's most valuable asset is its New York subsidiary, Israel Discount Bank of New York. The subsidiary is so valuable that some in the past suggested selling it in order to cover IDB's heavy losses in the communications sector. Press reports indicate that the Group is considering holding an issuance of Bank Discount New York on the Stock Exchange, in order to bring in money to expand the US subsidiary's activities.

5. (U) Other Details: Discount Group owns a number of leading Israeli financial affiliates and capital market institutions, including Israel Discount Capital Markets and Investments, Ilanot Discount, Israel Credit Cards and Diners Club, Mercantile Discount, 26.4% ownership in the First International Bank of Israel, and has holdings in one of the largest Israeli insurance companies, Harel. In addition to its subsidiary in New York, IDB has branches in Miami and Los Angeles.

The Sale

6. (U) The parties will complete the transaction the week of January 31, when the Bronfman group officially signs an agreement with MI Holdings, the GOI entity managing the sale. As IDB's foreign subsidiaries in the U.S. are included in the sale, the Federal Reserve Bank will have to give its approval for the sale, and the relevant European regulatory bodies will have to give their approval for the sale of European subsidiaries.

7. (U) The Bronfman group will pay NIS 1.05 billion at the time of closing and will receive financing from the State for NIS 250 million, which will be paid in 3 years, yielding an NIS 1.3 billion (USD 300 million) final price. The group has the option to purchase an additional 25 percent of the government's shares, on top of the 26% it is currently purchasing, within three years for a further NIS 1.25 bio. In a somewhat unusual twist to the deal, the GOI will receive additional sums depending on the bank's post-sale performance: If the bank's returns increase by 11 percent to 13 percent on average in the next four years, the Group will have to pay an additional NIS 78 million to NIS 156 million.

The Workers Have a Say

18. (SBU) IDB employs approximately 5,700 workers, the representatives of whom have been discussing the terms of sale with the Ministry of Finance for 8 months. These discussions have sometimes turned hot: The workers kept various branches of the Bank closed for days at a time during the last two months. Preliminary agreement between the workers and the MOF on January 5, which would entitle workers to receive NIS 250 million upon completion of the transfer of ownership to Bronfman, appeared to remove a large obstacle to the Bank's sale. This agreement also included a clause that current labor agreements would remain in place until 2009. Although the GOI is determined to complete the sale, labor action could slow down finalization of the deal.

GOI Proud of Sale

19. (U) Upon announcement of the deal January 23, Finance Minister Netanyahu issued a press release stating that the bank's future, private-sector owners would know how to manage the bank better and would strive to increase competition in the banking sector. The release also noted the GOI's objective to complete the privatization of all Israeli banks by the end of 2005, pointing directly to the privatization of Bank Leumi.

110. (U) Michal Abadi-Boyanjo, Chairman of MI Holdings, in an interview in the January 23/24 edition of Globes, said that she "is very happy that the process ended in a sale. The privatization of Discount is measured not only in terms of the price that is received, but also the influence of the sale on the bank and the entire banking system."
Kurtzer